



GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Fiscal Note 2009 Biennium

Bill #	SB0138	Title:	Prevent corporations from channeling income to insurance subsidiary
Primary Sponsor:	Wanzenried, D.	Status:	As Introduced

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|---|---|--|
| <input type="checkbox"/> Significant Local Gov Impact | <input type="checkbox"/> Needs to be included in HB 2 | <input type="checkbox"/> Technical Concerns |
| <input type="checkbox"/> Included in the Executive Budget | <input checked="" type="checkbox"/> Significant Long-Term Impacts | <input type="checkbox"/> Dedicated Revenue Form Attached |

FISCAL SUMMARY

	<u>FY 2008 Difference</u>	<u>FY 2009 Difference</u>	<u>FY 2010 Difference</u>	<u>FY 2011 Difference</u>
Revenue:				
General Fund	\$1,500,000	\$3,000,000	\$2,250,000	\$2,250,000
Net Impact-General Fund Balance	<u><u>\$1,500,000</u></u>	<u><u>\$3,000,000</u></u>	<u><u>\$2,250,000</u></u>	<u><u>\$2,250,000</u></u>

Description of Bill:

This legislation prevents non-insurance companies with an affiliate or subsidiary insurance company from transferring gains, assets or income to the insurance company in order avoid taxation under the preferential tax treatment available to insurance companies. Federal lawmakers recently enacted legislation to address this loophole at the federal level and this bill closes the loophole at the state level.

FISCAL ANALYSIS

Assumptions:

- Under current law, insurance companies are taxed under the state's premiums tax instead of the state's franchise or income tax. Under the premiums tax rules, certain gains on assets held by insurance companies and dividend payments from fully-owned insurance subsidiaries are not subject to tax. This preferential tax treatment is intended to provide stability to the insurance industry and ensure that insurance companies have sufficient asset growth to cover claims. The preferential tax treatment is unique to insurance companies and is not intended for use by non-insurance corporations. Other types of corporations are subject to the corporate income tax.
- This legislation will not change the preferential tax treatment given to insurance companies. Instead, this legislation prorates the dividends deduction that can be claimed by non-insurance parent companies on assets transferred to the insurance affiliate. The dividend deduction will be prorated by the capitalization percentage, which is based on the ratio of the premium income to total income of all insurance companies

in the commonly-controlled group. A high ratio of premium income to total income indicates the insurance company is predominately involved in the insurance business, and is not serving as a tax shelter.

3. This legislation also restricts the dividends-received deduction for any dividends attributable to premiums received by the insurance company from a member of the insurance company's commonly-controlled group. This provision ensures affiliated corporations are not paying excessive premiums to the insurance company in order to increase the capitalization percentage, thus increasing the deduction allowed.
4. The proposed legislation limits interest or expense deductions on property transferred to the insurance company by the non-insurance parent corporation for the purpose of tax-free accumulation of investment income. Further, transfers of appreciated property to an insurance company affiliate are recognizable and taxable gains in certain circumstances.
5. Finally, the proposed legislation restricts excessively-overcapitalized insurance companies and captive insurance companies from receiving preferential tax treatment by including the insurance affiliate's share of investment income, minus premiums-received income, in the non-insurance company parent's gross income if the insurance affiliate has less than 10% of its income from premiums (this percentage is 40% for predominately-captive insurance companies).
6. These provisions apply to tax years beginning after December 31, 2006.
7. The Department of Revenue (DOR) has identified 2-4 companies that will likely be subject to additional tax liability upon passage of this bill. The estimated liability increase per company is between \$500,000 and \$1 million.
8. DOR estimates the fiscal impact of this legislation is \$2.250 million in each fiscal year it is fully implemented, assuming 3 companies will be subject to an additional assessment of \$750,000.
9. Corporate license tax returns are due on or before the 15th day of the fifth month after the end of the tax year. However, an automatic six-month extension available for corporations, if requested, and additional extensions can be requested. Corporations reporting on a fiscal year basis, whose fiscal year begins December 1, would not be required to file until April 15th. With the automatic six-month extension the due date for the return is October 15th. Therefore, a corporation whose fiscal year began December 1, 2006 would not be required to file until October 15, 2008, which is in FY 2009. Corporations are responsible for making quarterly estimated payments which must be either 80% of the total tax shown on the return for the taxable year, or 100% of the total tax for the prior taxable year. For the purposes of this fiscal note, it is assumed that additional revenue from one of the three corporations projected by DOR to be subject to additional tax liability will be paid beginning in FY 2009. The additional revenue from the other corporations is assumed to be paid beginning in FY 2008. Therefore, revenue for FY 2008 will be \$1.5 million (\$2.250 million – \$0.750 million); FY 2009 revenue will be \$3.0 million (\$2.250 million + \$0.750 million); and FY 2010 and FY 2011 revenue will be \$2.250 million.
10. DOR will not incur any additional expenses due to passage of this legislation.

	<u>FY 2008 Difference</u>	<u>FY 2009 Difference</u>	<u>FY 2010 Difference</u>	<u>FY 2011 Difference</u>
<u>Fiscal Impact:</u>				
<u>Revenues:</u>				
General Fund (01)	\$1,500,000	\$3,000,000	\$2,250,000	\$2,250,000
<u>Net Impact to Fund Balance (Revenue minus Funding of Expenditures):</u>				
General Fund (01)	\$1,500,000	\$3,000,000	\$2,250,000	\$2,250,000

Sponsor's Initials

Date

Budget Director's Initials

Date